

November 9, 2016

Ex Parte

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: Business Data Services in an Internet Protocol Environment, WC Docket No. 16-143; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans, WC Docket No. 15-247; Special Access for Price Cap Local Exchange Carriers, WC Docket No. 05-25; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service, RM-10593.

Dear Ms. Dortch,

The Commission's fact sheet describes a conservative step toward addressing the broken market for business data services ("BDS"). The proposed order would apply rate regulation only to low-capacity DS1 and DS3 services, a marketplace characterized by a persistent and pervasive lack of competition across the entire country. Businesses, public interest groups, educators, and competitors have advocated for a more comprehensive approach that addresses competition failures in other BDS product markets as well, but with this proposal, the Commission is addressing the most extreme abuses of market power at this time. Sprint agrees that the FCC should move ahead with the proposed order.

Despite the Commission's discrete and conservative approach, AT&T and CenturyLink continue in their campaign to derail *any* meaningful relief to BDS customers, even in the most egregious situations. But the record strongly supports the Commission's proposal, leaving these companies without substantive support for their efforts to preserve their monopoly power. Their final gambit? A misleading, eleventh-hour demand to carve-out transport circuit elements from the reform framework—and thereby create an enormous loophole that, in effect, would eviscerate the order.

For the reasons outlined below, the Commission should reject this baseless attempt to muddy the water on transport circuit elements at the last moment. It should also reject the ILECs' arguments that the Commission's proposal to rationalize the DS1 and DS3 price caps would somehow reduce prices too much—in fact the proposal is extremely conservative and cuts price cap levels by far less than the record would support. Finally, the Commission should, within the proposal's framework, make a set of adjustments to the implementation schedule for the Order and to the relationship between wholesale and retail rates.

I. The Commission’s Proposal to Rationalize the DS1 and DS3 Price Caps is Well-Supported by the Record

A. Carving out transport rate elements would create a massive loophole and negate the impact of BDS reform on consumers.

In a set of misleading, eleventh-hour filings, AT&T and CenturyLink ask the Commission to carve out transport services from its price cap reform proposal.¹ This request is baseless. As described below, the exclusion sought by AT&T and CenturyLink (1) ignores the circuit-by-circuit analysis of market power that the Commission has conducted consistently throughout this proceeding; (2) neglects to account for the actual operation of the BDS marketplace; and (3) neglects the ILECs’ own pricing practices, which demonstrate that they exercise market power over entire DS1 and DS3 circuits—transport elements included. As a result, if the Commission were to carve out transport elements from its reform of the broken price cap system, it would allow the ILECs to evade even the conservative reductions in rates for BDS circuits that the Commission has determined would benefit consumers.

As an initial matter, it is important to recognize the limited type of transport facilities at issue under the BDS price cap regime. The special access transport services that are subject to the Commission’s price caps cover BDS circuit elements that provide “interoffice facilities . . . between the serving wire center and the LEC end office serving the end user.”² These interoffice transport circuit elements typically include channel mileage and, in some cases, multiplexing. They do not include entrance facilities, tandem-switched facilities, or direct-trunked transport facilities that are commonly referred to as “dedicated transport” in the context of delivering switched access services.³ And they do not include backbone or long-haul transit links that represent the bulk of competitive providers’ fiber networks. They cover the additional charges that BDS customers must pay in order to complete a BDS circuit—charges that typically are included in the unitary prices for Ethernet BDS offerings, as the Commission recognized in the *Further Notice*.⁴ As explained below, the record demonstrates that ILECs exercise market power over both the channel termination and interoffice transport elements of a BDS circuit.

¹ Letter from James P. Young, Counsel, AT&T, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Oct. 25, 2016) (“AT&T Oct. 25 Ex Parte”); Letter from Russell P. Hanser, Counsel, CenturyLink, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 at 1 (filed Oct. 28, 2016) (“CenturyLink Oct. 28 Ex Parte”); Letter from Russell P. Hanser and Brian W. Murray, Counsel, CenturyLink, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Nov. 4, 2016) (“CenturyLink Nov. 4 Ex Parte”).

² *Access Charge Reform*, CC Docket No. 96-262; *Price Cap Performance Review for Local Exch. Carriers*, CC Docket No. 94-1 et al., Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd. 14221 ¶ 10 (1999).

³ See 47 C.F.R. § 69.709 (a)(1)-(3) (describing switched access transport facilities).

⁴ *Business Data Services in an Internet Protocol Environment; Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans; Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform*

First, contrary to CenturyLink’s demonstrably false claim that “transport connections were removed entirely from Dr. Rysman’s analysis,”⁵ and AT&T’s similar claim that this entire proceeding has focused on channel terminations,⁶ the key market power analyses on the record cover both channel terminations *and* interoffice transport. Indeed, as part of the *2015 Data Collection*, the Commission requested billing information on all elements of a BDS circuit, including transport elements, such as channel mileage, that comprise the connection between a serving wire center and a LEC’s end office.⁷ To perform his market power analysis, Dr. Rysman used billing information from all reported circuit elements, including those related to interoffice transport. Indeed, rather than limiting his regression analyses to channel terminations alone—or removing transport entirely, as CenturyLink misleadingly claims—Dr. Rysman explicitly decided to “add up revenue” from all elements “to a single circuit and use the total circuit revenue to construct price.”⁸ As a result, Dr. Rysman analyzed the marketplace at the level of the full BDS circuit—including both channel termination and interoffice transport elements—and discovered that ILECs exercise market power for low-capacity BDS services. Dr. Baker, Mr. Zarakas, and Dr. Verlinda also conducted their regression analyses at the level of the full BDS circuit, and provided additional evidence of ILEC market power.⁹ Further, to conclude that ILECs control more than 80% of the BDS marketplace by revenue, Sprint’s economists analyzed total revenue associated with all elements that comprise a BDS circuit—which again include transport.¹⁰ Because all of these analyses relied on full circuit prices, the market failure that they revealed applies to both the channel termination and transport elements of a BDS circuit.

Second, the “needs of the [BDS] customer” and the manner in which “the [BDS] market operates today”¹¹ further establish that ILECs are able to charge supracompetitive rates for transport circuit elements—and not only channel terminations. Even though ILECs continue to

Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, Tariff Investigation Order and Further Notice of Proposed Rulemaking, FCC 16-54, 31 FCC Rcd. 4723 ¶ 282 (2016) (“*Further Notice*”).

⁵ CenturyLink Nov. 4 Ex Parte at 2.

⁶ AT&T Oct. 25 Ex Parte at 6-7.

⁷ See Data Collection Questions II.A.14 & II.B.6.

⁸ Dr. Marc Rysman, *Empirics of Business Data Services* (rev. June 2016) at 6 (“Rysman Rev. White Paper”). Cf. CenturyLink Nov. 4 Ex Parte at 3 (incorrectly claiming that Rysman “removed” transport connections “entirely” from his data set).

⁹ See Supplemental Reply Declaration of Jonathan B. Baker on Competition and Market Power in the Provision of Business Data Services ¶ 42 & n.3817 (dated Sept. 21, 2016; filed Sept. 22, 2016) (“Baker Sept. Supp. Reply Decl.”); Declaration of William P. Zarakas and Jeremy A. Verlinda at Appendix C, attached as Ex. D to Comments of Sprint Corporation, WC Docket No. 16-143 et al. (filed June 28, 2016).

¹⁰ Declaration of William P. Zarakas and Susan Gately ¶ 11(d), attached as Attach. 2 to Comments of Sprint Corporation, WC Docket No. 05-25 et al. (filed Jan. 28, 2016).

¹¹ *Further Notice* ¶¶ 282-83.

charge separately for transport and termination for legacy services, companies in the modern BDS marketplace typically buy transport and channel terminations together. There are several reasons why a customer purchasing an ILEC channel termination must also purchase transport elements from the ILEC. First, along many routes, competitive providers are simply unavailable. While CenturyLink insists that the construction of competitive fiber rings has fully addressed this issue,¹² that simply is not the case. Indeed, even if a competitive provider has a fiber ring in the area, which is not the case in many parts of the country, it does not follow that a competitor has deployed transport facilities to connect channel terminations to the relevant central offices in order to complete a given BDS circuit. Second, competitive transport, to the extent it exists, is typically offered only at very high capacities. While it is in theory possible to aggregate DS1 and DS3 channel terminations into higher capacity transport, there are significant practical limitations on such aggregation. Not every competitive transport provider permits these arrangements, and the central offices at issue must have enough DS1 or DS3 demand to fill the higher capacity transport connection. Third, in order to obtain any meaningful discount from the ILECs' excessive prices for channel terminations, customers must commit to very substantial minimum revenue requirements. In many cases, Sprint and others can only achieve those minimum levels by purchasing transport from an ILEC as well as channel terminations.

As these marketplace experiences make clear, competitive transport for DS1 and DS3 channel terminations is not a practical possibility for customers except in certain special situations. In the real world, purchasers that rely on an ILEC for channel terminations typically must also use the ILEC for interoffice transport.

Not only has the Commission recognized this,¹³ *but so has AT&T*. Indeed, in an attempt to justify exorbitant early termination penalties, AT&T informed the Commission that its BDS “[c]ustomers typically purchase channel terminations together with mileage or multiplexing.”¹⁴ In fact, AT&T reported that channel termination and transport circuit elements are purchased together so often that the Commission should analyze AT&T’s foregone revenue from a cancelled channel termination by averaging “revenues from channel terminations, mileage, and multiplexing” together¹⁵—which is exactly what the economists did to measure market power in this proceeding.

Thus, as the operation of the BDS marketplace makes clear, even if a number of competitors provide transport from the serving wire center to the relevant end office, the ILEC would still be able to charge unjust and unreasonable rates for the transport elements of a BDS circuit that terminates to an end-user location with no or inadequate competitive last-mile

¹² CenturyLink Nov 4. Ex Parte at 2.

¹³ *Further Notice* ¶¶ 282-83.

¹⁴ Reply of AT&T to Petitions to Reject or Suspend and Investigate Ameritech TN 1847, Pacific Bell TN 539, and Southwestern Bell TN 3428 (filed July 14, 2016).

¹⁵ *Id.*

facilities. As the Commission's data shows, these locations account for virtually the entire marketplace for DS1s, DS3s, and their Ethernet equivalents.¹⁶

Third, ILECs' actual pricing behavior provides direct evidence of the ILECs' ability to charge supracompetitive rates for transport circuit elements. As shown in the attached summary of ILEC tariffs,¹⁷ and as CenturyLink readily admits,¹⁸ ILECs typically charge more for DS1 and DS3 services in Phase II areas than they do in areas subject to price caps. Despite the incumbents' allegation that transport is abundantly competitive, this Phase II "premium" applies to both transport and channel termination circuit elements. Indeed, the average Phase II premium that Sprint pays is *greater* for DS1 and DS3 transport services than it is for DS1 and DS3 channel terminations.¹⁹ For example, while AT&T charges a Phase II premium of 2% to 8% for DS1 channel terminations offered at a 3-year term, it demands an 18% to 24% premium for DS1 transport elements—and the spread grows even wider for 5-year terms.²⁰ Similarly, CenturyLink's premium for 3-year, DS1 channel terminations ranges from 21% to 25%, but jumps to roughly 42% for transport.²¹ CenturyLink's Phase II premiums for DS3 transport are even more astounding: the ILEC charges a staggering 93% more for DS3 transport in Phase II areas than it does for DS3 transport in price cap areas, compared to an already unacceptable premium of 38% for DS3 channel terminations.²²

The overwhelming evidence of the ILECs' ability unilaterally to raise rates for transport sheds light on why the ILECs may be asking the Commission to exclude transport from the BDS reform plan at the eleventh hour. Removing transport from Phase I price caps would create an enormous loophole that would allow incumbents to maintain their monopoly rates. With this change, the ILECs would be able to simply raise DS1 and DS3 transport prices to offset any price cap reductions for channel terminations, thereby ensuring that the total BDS price for a circuit remains at the profit-maximizing level for the ILEC and eliminating any benefits that price cap reductions would have for those BDS consumers. The Commission should not fall into this trap, and should apply its price cap reforms to both channel termination and transport elements of a BDS circuit.

¹⁶ See *infra* notes 23-24 & accompanying text.

¹⁷ See Average Increase in ILEC Tariffed Rates for Channel Termination and Transport Circuit Elements in Phase II Areas, appended hereto as Attachment A.

¹⁸ See CenturyLink Oct. 28 Ex Parte at 1.

¹⁹ See Attachment A.

²⁰ *Id.*

²¹ *Id.*

²² *Id.*

B. The decision to apply price caps nationwide is the right decision and fully supported by the record.

The Commission has proposed to grant Phase I pricing flexibility everywhere in the country, including both areas that do not currently benefit from any form of pricing flexibility and Phase II areas where ILECs are exempt from price caps. Not only is the application of price caps on a nationwide basis reasonable, it is the only rational means of regulation in light of the record's findings that nearly the entire country lacks adequate competition for DS1 and DS3 services.

As Dr. Rysman found, 99% of all BDS locations are served by a duopoly at best—and a staggering 77% are subject to a BDS monopoly.²³ These competition findings are extraordinarily consistent across economists.²⁴ Remarkably, they address actual competition for BDS *at all capacities*, and not just the least competitive, low-capacity services to which the Commission's price cap system would apply. As a result, the state of competition for DS1s and DS3s is even worse than these already bleak numbers suggest. Importantly, the record also demonstrates that potential competition is unable to protect consumers from these DS1 and DS3 monopolies and duopolies. The Commission asked the industry to describe its rules for building out their networks to reach new customers, and the response was clear: no companies are deploying new DS1s and DS3s, and competitors are not even building out Ethernet to serve locations with BDS at DS1- and DS3-level capacities.²⁵ Regression analyses confirm the

²³ Rysman Rev. White Paper at 15, Table 7.

²⁴ Dr. Jonathan Baker determined that 98% are served by at most a duopoly, and, like Dr. Rysman, concluded that 77% of customer locations are subject to a BDS monopoly. *See* Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services ¶ 44, WC Docket No. 05-25 et al. (filed Jan. 27, 2016; revised public version submitted on Apr. 14, 2016). Similarly, Drs. Besen and Mitchell found that 97% of locations are served by at most two providers, and 73% are served by just one provider. *See* Declaration of Stanley M. Besen and Bridger M. Mitchell ¶¶ 25- 26 & Table 1 (“Besen/Mitchell Decl.”), appended as Attachment 1 to Comments of Sprint Corporation, WC Docket No. 05-25 et al. (filed Jan. 27, 2016; revised public version submitted on Apr. 11, 2016).

²⁵ For example, Level 3 has explained that it is “infrequently the case that Level 3 can deploy a new fiber connection to serve a customer demanding only 100 Mbps of bandwidth or below[. . . because the distance between a customer location and a splice point . . . usually exceeds the construction feasibility limits.” Declaration of John Merriman on Behalf of Level 3 Communications, Inc. ¶ 6, appended to Comments of Birch Communications, Inc., EarthLink, Inc., and Level 3 Communications, LLC, WC Docket No. 16-143 et al. (filed June 28, 2016). Similarly, TDS reports that “a fiber lateral build to any customer located 100 to 1,000 feet from the nearest splice point on TDS CLEC’s fiber network is not competitive at speeds ranging from 10 to 100 Mbps because TDS CLEC could not recover its required revenue and compete with lower RBOC retail rates.” Reply Comments of TDS Metrocom, LLC at 2, 15, WC Docket No. 05-25 et al. (filed Feb. 19, 2016). Windstream similarly reports that “a single 100 Mbps circuit almost never generates the amount of revenue

absence of a material competitive effect from potential competitors, and that actual, in-building competition acts as the most effective constraint on ILEC pricing.²⁶

The record on ILEC pricing behavior also confirms the presence of nationwide market power for low-capacity BDS services, even if there are a very small percentage of individual locations where effective competition may exist. For example, CenturyLink recently asserted that its practice is to charge much higher rates for DS1 and DS3 services in Phase II areas than it does in price cap areas.²⁷ As shown in the attached summary, this practice is not unique to CenturyLink—and is in fact pervasive across all ILECs.²⁸ But existing price cap levels are already too generous, and allow ILECs to price BDS above rates that would prevail in a competitive marketplace. And ILECs, including CenturyLink, continue to price BDS at the maximum rates allowed under existing caps where they apply.²⁹ As a result, CenturyLink’s statement that it charges more in Phase II areas amounts to an admission that CenturyLink, like AT&T and Verizon, charges supracompetitive rates for DS1 and DS3 services in *both* regulated *and* deregulated areas—in other words, in all locations throughout its incumbent territory. Along the same lines, AT&T’s and Verizon’s decisions to impose across-the-board price increases in response to the Commission’s *Tariff Investigation Order* also reveal that competitive market forces are inadequate throughout these ILECs’ service areas.³⁰

required to justify deployment of a new last-mile connection by its competitive carrier operations, even when Windstream has already deployed fiber feeder in the customer’s vicinity.” Declaration of David Schirack and Mike Baer ¶ 16, appended as Attachment A to Comments of Windstream Services, LLC, WC Docket No. 16-143 et al. (filed June 28, 2016). Moreover, the CostQuest study on the hurdles that providers face in deploying BDS offerings filed in this proceeding concludes that “an economically rational CLEC will not self-deploy to serve a single customer with less than 1 Gbps of capacity per building even if [the] building offers a more attractive option than wholesale lease payments . . . because the revenue hurdle is higher than the crossover point in the build-versus-buy analysis.” CostQuest White Paper #1, appended as Attachment A to Letter from Jennie B. Chandra, Vice President of Public Policy and Strategy, Windstream Corporation, to Marlene H. Dortch, Secretary, FCC (filed June 8, 2015).

²⁶ Baker Sept. Supp. Reply Decl. ¶ 2 (“Contrary to what IRW assert, however, potential competition from nearby rivals is not sufficient to constrain ILECs to price business data services competitively. Accordingly, the possibility of potential competition does not undermine the inference of ILEC market power derived from Prof. Rysman’s observation that nationwide, 77.2% of buildings have a single in-building provider (almost always an ILEC) and almost all the rest (21.8%) have only two in-building providers”); *see also* Rysman Rev. White Paper at 3, 22-23.

²⁷ *See* CenturyLink Oct. 28 Ex Parte at 1.

²⁸ *See* Attachment A.

²⁹ *Further Notice* ¶ 240.

³⁰ *See* Verizon Telephone Companies, Tariff F.C.C. Nos. 1, 11, 14 and 16, Transmittal No. 1335, Description and Justification at 4 (July 1, 2016). *See also* Ameritech Operating

This evidence is consistent with Sprint’s analysis of its experience with ILEC and CLEC pricing, which shows enormous rate disparities across markets, even at higher capacities, and even in urban areas.³¹ It is also consistent with the nationwide studies of market power for low-bandwidth TDM services conducted by Dr. Rysman and Dr. Baker. As Dr. Rysman concluded, “competitive supply in a unique location is correlated in both statistically and economically significant ways with lower ILEC prices for DS1s and DS3s at that location.”³² Dr. Baker quantified the reduction more precisely, and concluded that DS1 and DS3 rates fall from 25% to as much as 51% as ILECs face greater in-building competition.³³ Importantly, these analyses do more than corroborate the economists’ findings on market concentration and actual competition (or the lack thereof). They also dispel the notion that potential competition is having a significant impact anywhere in the marketplace. Indeed, the benefit of potential competition is that the possibility of entry in the future will discipline rates now—but clearly, the pricing data shows that the entry barriers reported by competitors are too insurmountable to constrain ILEC rates for low-capacity BDS circuits.

When all but a few locations across the country are monopolies or duopolies, and where ILEC market power exists throughout the Nation, the appropriate—and indeed only rational—policy response is to apply uniform rules across the country. Importantly, this does not mean that the FCC must conclude that every single building in the country is not competitive. The Commission should permit ILECs the opportunity to demonstrate, through waiver requests, that competition is adequate at any of the tiny percentage of locations that have or develop adequate competition for low-capacity TDM BDS, and excuse them from price caps in these locations.

C. An 11% one-time reduction and 3% X-factor are very conservative—and if anything, should be *higher*.

The Chairman’s fact sheet proposes to apply an 11% one-time adjustment in TDM price caps and an X-factor of 3% each year. These amounts represent a very conservative approach that is very generous to the ILECs and more than adequately supported by the record.

Companies Tariff F.C.C. No. 2, Transmittal No. 1847 et al., Petition of Windstream Services, LLC to Reject or Suspend and Investigate at 2 (filed July 8, 2016) (“If allowed to take effect AT&T would, de facto, force a huge price increase on wholesale purchasers, and, in turn, on retail customers.”); Ameritech Operating Companies Tariff F.C.C. No. 2, Transmittal No. 1847 et al., Petition of Birch Communications, Inc., EarthLink, Inc., INCOMPAS, Level 3 Communications, LLC, Sprint Corporation, and Windstream Services, LLC to Reject or Suspend and Investigate (filed July 8, 2016) (explaining why AT&T’s proposed elimination of circuit portability would result in an effective increase in rates for wholesale purchasers).

³¹ See Letter from Charles W. McKee, Sprint Corporation, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 (filed Oct. 17, 2016).

³² *Further Notice* ¶ 238; Rysman Rev. White Paper at 3, 22-23.

³³ Baker Sept. Supp. Reply Decl. ¶ 17.

As an initial matter, the Commission's own price cap adjustment and X-factor calculations from the *Further Notice* are higher than the 11% and 3% figures in Chairman's proposal. In the *Further Notice*, the FCC calculated the one-time adjustment and X-factor three separate ways.³⁴ Averaging these three results for the time period from 1997-2013 results in a one-time adjustment of almost 13% and an X-factor well above 3%.

In addition, Sprint has provided a more than reasonable basis for adopting a one-time adjustment and X-factor that exceed 11% and 3% respectively by an even larger amount than the Commission's initial calculations. In late August, Chris Frentrup, who co-authored one of the original FCC studies of productivity when price cap regulation was adopted in 1990, and David Sappington, former FCC Chief Economist, submitted a declaration building on the FCC's Connect America Cost Model approach to determining the one-time reduction and X-factor.³⁵ Put differently, Drs. Frentrup and Sappington simply used the FCC's own methodology and enhanced it to account for certain economic nuances that were not included in the FCC's initial assessment. After doing so, Frentrup and Sappington calculated a one-time adjustment of *at least* 17.1% and an initial X-factor of at least 3.94%.³⁶ Predictably, the ILECs immediately critiqued this filing, although the incumbents did not actually calculate how the numbers would change after correcting the purported errors they identified.³⁷ In early October, Sprint did so, and found that the net effect of incorporating each of the incumbents' critiques was an *increase* in the estimated one-time adjustment to 20.5% and the X-factor to 4.31%.³⁸ And even Verizon agrees with figures that are higher than those proposed in the Chairman's fact sheet, as it has advocated for a one-time adjustment of 15% and an X-factor of 4.4% minus inflation.³⁹ Against this backdrop, it is remarkable that AT&T and CenturyLink advocate for an X-factor of 1.81% and 2%, respectively.⁴⁰ It is even more stunning that CenturyLink argues that 11% would be "far outside the range permitted by the record evidence,"⁴¹ while AT&T asserts that appropriate

³⁴ *Further Notice* ¶¶ 404-415.

³⁵ Declaration of Chris Frentrup and David Sappington, WC Docket No. 16-143 et al. (filed Aug. 31, 2016).

³⁶ *Id.* ¶¶ 16, 20.

³⁷ See Supplemental Declaration of Mark E. Meitzen, Ph.D. and Philip E. Schoech, Ph.D., attached to Letter from Christopher T. Shenk, Counsel for AT&T, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Sept. 22, 2016).

³⁸ Letter from Chris Frentrup, Sprint Corporation, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Oct. 5, 2016).

³⁹ See, e.g., Letter from Kathleen Grillo, Verizon, and Chip Pickering, INCOMPAS, to Marlene H. Dortch, Secretary, FCC, at 1, WC Docket No. 16-143 et al. (filed Aug. 9, 2016); Reply Comments of Verizon at 9-10, WC Docket No. 16-143 (filed Aug. 9, 2016).

⁴⁰ CenturyLink Oct. 28 Ex Parte at 4; AT&T Oct. 25 Ex Parte at 2.

⁴¹ CenturyLink Oct. 28 Ex Parte at 2.

estimates support “no material one-time adjustment.”⁴² There is no reliable record support for these positions.

To the extent AT&T and CenturyLink continue to claim that meaningful TDM rate reductions would undercut investment and innovation, the Commission should reject these assertions as well. As an initial matter, AT&T and CenturyLink express a relationship between TDM rate reductions and investment incentives that is exactly backward. The ILECs’ continued ability to extract monopolist rents from their legacy networks artificially blunts marketplace incentives that, in a competitive environment, would encourage them to upgrade more rapidly to more efficient IP-based technology. Thus, if the Commission succeeds in limiting the ILECs’ ability to charge supracompetitive rates for legacy DS1 and DS3 services, the effect would be to *accelerate* investment and innovation in next-generation wireline networks.

More importantly, recent marketplace activity demonstrates that both AT&T and CenturyLink are fully capable of investing in their networks without charging their customers unjust and unreasonable rates for BDS. AT&T has announced a deal to acquire Time Warner for more than \$85 billion—nearly half of which AT&T will provide in cash. Similarly, CenturyLink’s pending \$34 billion acquisition of Level 3 in a cash-and-stock deal, as well as its recent financial performance, belie the assertion that the company’s crushing debt burden would force it to reduce investment if it were to charge lawful rates for BDS. Indeed, as both INCOMPAS and Windstream observe, CenturyLink’s CFO boasts that BDS is a “high margin” offering,⁴³ and the company’s earnings results and SEC filings likewise show no evidence that CenturyLink is experiencing BDS cost increases.⁴⁴ To the contrary, CenturyLink’s net operating

⁴² AT&T Oct. 25 Ex Parte at 2.

⁴³ CenturyLink, FQ1 2016 Earnings Call Transcripts at 11 (May 4, 2016), <http://ir.centurylink.com/Cache/1500085040.PDF?Y=&O=PDF&D=&fid=1500085040&T=&iid=4057179>; see Letter from Karen Reidy, Vice President, Regulatory, INCOMPAS, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (Aug. 24, 2016) (“INCOMPAS Aug. 24 Ex Parte”); Letter from Malena H. Barzilai, Windstream, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (Sept. 22, 2016) (“Windstream Sept. 22 Ex Parte”).

⁴⁴ As INCOMPAS summarizes:

CenturyLink’s SEC financial reports for 2005 (the year price caps were frozen under CALLS) through 2015 shows no evidence that CenturyLink is experiencing BDS cost increases. Instead, these reports demonstrate that, on a per subscriber basis, CenturyLink’s revenues are 18 percent higher, and its margins are 32 percent higher. So while the company’s recent letter attempts to convince the Commission that its BDS business is struggling, it is telling investors that business is booming. Astoundingly, CenturyLink’s 2015 shareholder payout was 416 percent higher than it was in 2005 for CenturyTel, Embarq, and Qwest.

INCOMPAS Aug. 24 Ex Parte.

income *for BDS* is up 47%.⁴⁵ The self-serving cost model that CenturyLink recently filed hardly undercuts the rosy picture of its BDS offerings that the company continues to paint for its investors, as it employs cherry-picked comparisons to create a skewed view of the overall result of the Commission’s proposed reforms.⁴⁶ Indeed, CenturyLink only compares DS1 “costs” to the average revenue from a tariffed, three-year term DS1 offering, and did not include a comparison for month-to-month rates or any information about DS3s at all.⁴⁷

Finally, CenturyLink’s allegations about non-compensatory rates, if true, are the result of its own pricing strategy—and not price cap regulation. For example, CenturyLink complains that its rates are averaged over large geographic areas, but fails to mention that under the FCC’s price cap rules it has the option of de-averaging its BDS rates into pricing zones. More importantly, to the extent the price caps *actually* result in rates that are below costs, CenturyLink has the option to seek approval for above-cap rates pursuant to the Commission’s existing price cap rules.⁴⁸

II. The Commission Should Take Steps to Ensure that the Order and Second Further Notice Meaningfully Impact BDS Competition

The key elements of the reform proposal outlined in the Chairman’s fact sheet represent an administrable path toward rationalizing rates for DS1 and DS3 services. But certain details will make the difference between rules that make a real-world improvement for BDS buyers and rules that make only paper changes. The Commission should therefore make the following adjustments to the proposal.

First, the Commission should require the industry to transition to just and reasonable rates over a period no longer than two years, beginning as soon as possible. The record is clear that each week of delay in bringing lawful rates to the marketplace costs BDS customers millions of dollars—and imposes even greater costs to the economy at large.⁴⁹ In addition, the Commission should adopt Sprint’s common-sense implementation proposal to ensure that its reforms result in real-world cost reductions for all customer classes.⁵⁰

⁴⁵ Windstream Sept. 22 Ex Parte at 2.

⁴⁶ See Declaration of Peter B. Copeland, attached to Letter from Craig J. Brown, CenturyLink, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Sept. 27, 2016).

⁴⁷ *Id.*

⁴⁸ See 47 C.F.R. § 61.41(e).

⁴⁹ See Letter from Karen Reidy, Vice President, INCOMPAS, to Tom Wheeler, Chairman, FCC, at 1, WC Docket No. 16-143 et al. (filed July 28, 2016) (summarizing WIK-Consult study showing that “[T]he pricing of [BDS] has a critical impact on the economy as a whole . . . reasonable price reductions for these services would have ‘spill-over effects that multiply the benefits to the broader society’”).

⁵⁰ See Letter from Charles W. McKee, Vice President, Government Affairs, Federal & State Regulatory, Sprint Corporation, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-

Second, while Sprint supports moving ahead with reform of only the TDM marketplace now, the Commission should ensure that the few Ethernet-related elements of the Order are effective and do not tie the hands of a future Commission. The record is clear that Ethernet BDS is essential to next-generation broadband networks⁵¹ and to the schools, universities, and start-ups that function as the laboratories of U.S. innovation.⁵² Accordingly, the Order should (1) ensure that wholesale BDS rates are priced *below* retail rates; (2) reject the pleas of CenturyLink and AT&T to remove scrutiny of the unreasonable Ethernet pricing practices described in the fact sheet; (3) describe the full range of analysis of the marketplace for Ethernet BDS presented in the record; and (4) preserve the interim protections adopted in the *Technology Transitions Order* until Ethernet rates are fully addressed.

In the Second Further Notice, the Commission should commit to further exploring the record on the Ethernet marketplace, especially in light of the industry’s recent step toward further consolidation. Indeed, the Vertical Systems Group Ethernet “Leaderboard” touted by AT&T and CenturyLink as evidence of vibrant Ethernet competition would radically change as a result of the pending acquisitions announced this year. As industry observers have reported, CenturyLink’s acquisition of Level 3 “will create arguably the third largest domestic enterprise service player” behind AT&T and Verizon⁵³—and allow ILECs to continue to control the lifeblood of tomorrow’s wireless and wireline networks. To facilitate continued review of Ethernet competition, the Commission should seek comment on the addition of BDS to the list of services for which facilities-based carriers report census-block-level information on the FCC’s Form 477. The Commission should also seek comment on streamlined methods for gathering

143 et al., at 3-7 & Attachment A (filed Oct. 21, 2016) (proposing rule to ensure all BDS customers benefit from DS1 and DS3 rate reductions).

⁵¹ See, e.g., Reply Comments of Competitive Carriers Association at 3, WC Docket No. 16-143 et al. (filed Aug. 9, 2016); Letter from Steven K. Berry, President & CEO, Competitive Carriers Association, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 16-143 et al. (filed Sept. 9, 2016); Reply Comments of Sprint Corporation at 40, 48-53, WC Docket No. 16-143 et al. (filed Aug. 9, 2016); Comments of INCOMPAS at 11-12, WC Docket No. 16-143 et al. (filed June 28, 2016).

⁵² See, e.g., Letter from John Windhausen, Jr., Executive Director, SHLB Coalition, to Tom Wheeler, Chairman; Mignon Clyburn, Commissioner; Jessica Rosenworcel, Commissioner; Ajit Pai, Commissioner; Michael O’Rielly, Commissioner, FCC, at 4-5, WC Docket No. 16-143 (filed Oct. 18, 2016); Letter from John Windhausen, Jr., Executive Director, SHLB Coalition, to Marlene H. Dortch, Secretary, FCC, at 1, WC Docket No. 16-143 et al. (filed Aug. 19, 2016); SHLB Coalition, *Connecting Anchor Institutions: A Broadband Action Plan* at 1-14 (2016), https://ecfsapi.fcc.gov/file/1081945436307/Broadband%20Action%20Plan_SHLB.pdf.

⁵³ Sean Buckley, *CenturyLink-Level 3: A \$34B deal that creates a global fiber powerhouse, threatening AT&T, Verizon*, FIERCETELECOM (Oct. 31, 2016, 1:19PM), <http://www.fiercetelecom.com/telecom/centurylink-level-3-34b-deal-creates-a-global-fiber-powerhouse-threat-to-at-t-verizon>.

Ethernet pricing information, including the submission by purchasers and sellers of BDS rates in their three largest Ethernet contracts by revenue. By building on existing reporting requirements, the Commission can drastically reduce any burden that much-needed continued examination of the BDS marketplace might have on the industry.

Sincerely,

A handwritten signature in blue ink, appearing to read "Paul Margie".

Paul Margie
Counsel to Sprint Corporation

Encl.

ATTACHMENT A

**AVERAGE INCREASE IN ILEC TARIFFED RATES FOR CHANNEL
TERMINATION AND TRANSPORT CIRCUIT ELEMENTS IN PHASE II AREAS**

DS1				
Channel Termination				
	3 Year Term		5 Year Term	
	Urban	Rural	Urban	Rural
Verizon	17%	28%	17%	28%
AT&T	2%	8%	2%	8%
CenturyLink (Qwest only)	25%	21%	21%	21%
Dedicated Transport (10 miles)				
	3 Year Term		5 Year Term	
	Urban	Rural	Urban	Rural
Verizon	45%	45%	44%	44%
AT&T	18%	24%	21%	27%
CenturyLink (Qwest only)	42%	42%	41%	41%

DS3				
Channel Termination				
	3 Year Term		5 Year Term	
	Urban	Rural	Urban	Rural
Verizon	33%	33%	33%	33%
AT&T	19%	19%	17%	16%
CenturyLink (Qwest only)	38%	38%	39%	39%
Dedicated Transport (10 miles)				
	3 Year Term		5 Year Term	
	Urban	Rural	Urban	Rural
Verizon	25%	25%	25%	25%
AT&T	10%	13%	17%	23%
CenturyLink (Qwest only)	93%	93%	109%	109%